(33)

No. 92-1384

In the Supreme Court of the United States

OCTOBER TERM, 1993

BARCLAYS BANK PLC,
Petitioner,

v.

FRANCHISE TAX BOARD,
AN AGENCY OF THE STATE OF CALIFORNIA,
Respondent.

On Writ of Certiorari to the Court of Appeal of the State of California in and for the Third Appellate District

AMICUS CURIAE BRIEF ON BEHALF OF THE STATES OF ALASKA, MONTANA, NEW HAMPSHIRE, AND OREGON, IN SUPPORT OF RESPONDENT FRANCHISE TAX BOARD

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INTERESTS OF *AMICI CURIAE*

The States that have joined in this *amicus curiae* brief in support of the respondent State of California Franchise Tax Board all have utilized the unitary business principle and formula apportionment to tax the net incomes of multistate and multinational corporations which conduct business in each State. None of the *amici* utilizes the Arms Length/Separate Accounting method. The State of Alaska applies worldwide combined reporting as the required method of income tax reporting for certain classes of taxpayers,[1] and other of the *amici* States have utilized the worldwide unitary reporting system in prior tax years, or do so pursuant to taxpayer election.[2]

Even States that have in recent years modified the precise worldwide apportionment formula under attack in these petitions nevertheless have significant tax revenues at risk because that formula was applied in prior years for which there are still open tax proceedings. In some cases, these open tax cases date back many years.[3] As a result, cumulatively, billions of dollars are at stake for the States.[4] Even if it is assumed that the *amici* could make

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[1] Alaska Stat. § 43.20.072 applies the worldwide unitary method to taxpayers engaged in the production of oil and gas from leases or property within the State of Alaska, as well as to taxpayers engaged in the transportation of oil or gas by pipeline within the State.

[2] Montana utilizes the worldwide combined reporting method, but also has a "water's edge election" available to taxpayers. Mont. Stat. § 15-31-301 *et seq.* New Hampshire and Oregon both assessed taxes on unitary businesses on a worldwide combined reporting basis prior to 1986. Since then, each State has applied a specific "water's edge" formulation. *See* N. H. Stat. § RSA 77-A, *amended by* § RSA 77-A:2-b (Ch. 153:4, N. H. Laws of 1986). *See also* Or. Rev. Stat. § 314.363, *amended by* § 317.715 (eff. January 1, 1986).

[3] In the case of Alaska, for example, there are open state tax proceedings pending under the worldwide unitary method which include up to twelve years of prior tax assessments, dating back to 1982.

[4] The *amici* all have open taxpayer proceedings which involve prior years' assessments under the worldwide unitary method. The dollars at risk in the different States range from a low of approximately three and one-half million dollars to a high of well in excess of five hundred million. California, of course,

(continued...)

changes in their tax statutes to cure any constitutional defects found by this Court, the matter of taxes already assessed for prior years might not be resolved by such changes. Thus, the refund claims which would surely result from a reversal of the California courts' decisions could disrupt States' finances significantly.

In addition to their direct fiscal interests, the *amici* States all have broader interests in retaining the authority and the flexibility, which has not been circumscribed by Congress, to adopt reasonable apportionment methods and to make changes in their statutory tax structures over time as needed to address their fiscal and administrative needs.[5] Indeed, it was largely because of the administrative difficulties and costs inherent in applying the separate accounting tax method to modern multistate and multinational corporations that almost all States have turned from it to the unitary method for taxing such businesses since World War II.[6] If the Court accepts the petitioners' arguments that national uniformity interests in the separate accounting method rise to the level of a constitutional requirement, the *amici* States' ability to continue to apply reasonable, cost-effective unitary tax systems to meet changing business realities would be stymied. The *amici* States have a strong interest in avoiding such a costly and inefficient result.

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[4](...continued)
has already indicated that it stands to lose over four billion dollars in tax revenues if its worldwide unitary tax scheme is invalidated. Barclays Supp. Br., at 1; Resp.. Br. in Opp. to Cert. in *Colgate-Palmolive*, at 15.

[5] *See* I J. Hellerstein & W. Hellerstein, State Taxation, ¶ 8.03 at 8-29 (2d ed. 1993) (hereinafter cited as "Hellerstein Treatise"). Individual States have adopted variations and refinements of the formula apportionment model, and, as a result, even though the general rule of the unitary business principle is adhered to by nearly all States, no two State tax laws are completely identical. *Id.*, ¶ 9.06 at 9-23, & n. 72.

[6] The Hellerstein Treatise reports that forty-five of the forty-six States (including the District of Columbia) that levy corporate income taxes have adopted some version of the unitary formula apportionment method to apply to multistate and multinational businesses. Hellerstein Treatise, ¶ 9.02, Table 9.1 at 9-8; ¶ 9.06 at 9-23.

SUMMARY OF ARGUMENT

There are few powers more fundamental to State sovereignty than the power to tax. This case involves a challenge to the exercise by California of a prerogative incident to that power, the choice of a rational, administratively appropriate, and neutrally applied method of apportioning the income of a multinational company conducting substantial business in the State. The method chosen by California is based on sound tax accounting valuation concepts that this Court has upheld for more than 70 years: the unitary business principle. Furthermore, in *Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159 (1983), the Court upheld that very California tax method against Foreign Commerce Clause challenges brought by a United States multinational corporation with foreign subsidiary operations.

Thus, Barclays' challenge to the California tax, at its core, rests on the argument that unitary taxation is constitutionally more offensive when applied to a multinational corporation with a parent organized in the United Kingdom, because many nations do not use worldwide unitary taxation and at least the prior Administration of our Federal Government opposed the use of that taxation method by the States on "policy" grounds.

Amici believe that Barclays' arguments are squarely foreclosed by this Court's decision in *Wardair Canada Inc. v. Florida Dept. of Revenue*, 477 U.S. 1 (1986). Here, as in *Wardair*, Congress must be considered, by "negative implication," to have approved the challenged State tax. The facts in this case are remarkably similar to those in *Wardair*. In both *Wardair* and this case, certain foreign nations and business interests, as well as the Executive (in some Administrations), complained that a State tax was contrary to established international "practices," which, the taxpayer argued, reflected "federal policy." However, the relevant international conventions into which the United States has entered, including conventions with the "home" country of the company challenging the tax, do <u>not</u> prohibit the challenged State tax. And the record concerning Congressional lawmaking conduct in the area reflected, at a minimum, Congress' willingness to tolerate the State tax, its "acquiescence." The Court should defer to that Congressional tolerance in this case, as it did in *Wardair*.

Barclays' argument can only be termed extreme in its implications. Barclays suggests that when the Congress has chosen not to take action to preempt, by treaty or legislation, State tax laws viewed by some here and abroad as misguided or burdensome, the Court should fill that legislative void, evaluate foreign policy concerns, and impose as constitutional law a particular form of tax accounting preferred by some foreign governments and business interests. However, the Court has never assumed the role of enforcer of uniformity among the States as to all matters implicating foreign relations. Given the decisions by Congress over more than 20 years not to impose such tax apportionment uniformity on the States, the Court obviously should decline to do so here. Congress has been well aware of the controversy concerning the unitary State taxation method and has not preempted the States despite the clear opportunity to do so.

Barclays is attempting to circumvent the tax treaty between the United States and its "home," the United Kingdom, which clearly allows the State tax of which Barclays complains. Barclays asks the Court to do by way of constitutional law what no act of Congress, treaty, or even executive agreement, has done: to abrogate State taxation rights in the interests of one "policy" view. For the reasons discussed in this brief, the Court should decline that invitation based on its recent precedents and on fundamental precepts of federalism and separation of powers.

ARGUMENT

I. UNITARY BUSINESS APPORTIONMENT HAS LONG BEEN A CONSTITUTIONALLY ACCEPTED METHOD FOR STATE TAXATION OF MULTISTATE AND MULTINATIONAL CORPORATIONS.

Barclays is mistaken to suggest that California's use of the unitary corporate income taxation method represents a recent "intrusion" inconsistent with historical practices and shocking to the international business community. Barclays' Br. 23. This Court recently explained that the "unitary business principle . . . is not a novel construct, but one which [it] approved within a short time after the passage of the Fourteenth Amendment's Due Process Clause." *Allied-Signal, Inc. v. Director, Div. of Taxation*, 112 S.Ct. 2251, 2258 (1992).

In *Allied-Signal*, the Court traced the development of the unitary business principle from the late 1800's, when States first began to recognize that there was value in enterprises like railroads and telegraph companies which transcended the worth attributable to their particular property segments located within a State's borders. *Id.* at 2258. In a series of cases beginning in 1897, the Court found that "a State could base its tax assessments upon 'the proportionate part of the value resulting from the combination of the means by which the business was carried on, a value existing to an appreciable extent throughout the entire domain of the operation.'" *Allied-Signal*, 112 S.Ct. at 2258, *quoting Adams Express Co. v. Ohio State Auditor*, 165 U.S. 194, 220-21 (1897).

The unitary business principle was extended to States taxation of corporate income in *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 120-21 (1920). Only four years later, the Court decided *Bass, Ratcliff & Gretton, Ltd v. State Tax Comm'n*, 266 U.S. 271 (1924), where it extended the unitary principle to the worldwide income of a foreign-domiciled corporation which did its manufacturing abroad but had sales in the United States. *Bass* relied, in turn, on *Wallace v. Hines*, 253 U.S. 66 (1920), which had recognized, in the context of an excise tax, that a State may look to the property of a foreign corporation beyond its borders to "get the true value of the things within it, when they are part of an organic system of wide extent," giving the local property a value above that which it might otherwise possess. *Wallace*, 253 U.S. at 69, *cited in Bass*, 266 U.S. at 282.

These early cases provided the doctrinal foundation upon which States began to rely to apportion the income of unitary businesses. Never, since the 1920's, has the Court suggested that any line must be drawn between multistate and multinational enterprises insofar as the unitary business principle applies. As long as a corporation and its foreign affiliates are truly unitary, a State has a sufficient connection with the whole enterprise to legitimately tax a fair share of the income of the whole attributable to its in-State activities.

The Court reaffirmed the application of the unitary principle to a multinational corporation with foreign subsidiaries in *Mobil Oil Corp. v. Comm'r of Taxes of Vermont*, 445 U.S. 425 (1980), which

held that the unitary principle is "the linchpin of apportionability in the field of state taxation." *Id.* at 439. Mobil challenged Vermont's inclusion of the "foreign source" dividend income of Mobil's subsidiaries domiciled in other countries within the unitary tax base for purposes of Vermont's apportionment formula. The *Mobil* decision repudiated the notion that the foreign source of the corporate income rendered it untaxable. Citing *Bass*, the Court held that it "has applied the same [unitary-business] rationale to businesses operating both here and abroad . . . ." *Mobil*, 445 U.S. at 438. Rejecting the taxpayer's argument that the source of the income was determinative, the Court ruled that the unitary nature of the underlying business, and not the corporate form, was critical. *Id.* at 440.

California's use of the unitary business principle was specifically upheld as applied to the income of foreign-based subsidiaries of a multinational corporation in *Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159 (1983). In *Container*, the Court noted that it had "long ago upheld the constitutionality of the unitary business/formula apportionment method, although subject to certain constraints. The method has now gained wide acceptance, and is in one of its forms the basis for the Uniform Division of Income For Tax Purposes Act ...." *Id.* at 165.[7]

Most recently in *Allied-Signal, Inc. v. Director, Division of Taxation*, 112 S. Ct. 2251 (1992), the entire Court reaffirmed the constitutionality of the unitary business principle as a viable, and even preferred, method for distinguishing between income generated within a State, which is taxable, and income generated without, which is not. *Id.* at 2261-63. In light of the long history of consistent approval of the unitary method, the Court in *Allied-Signal* concluded: "Indeed, if anything would be unworkable in

[7] By the 1950's, so widely embraced by States was the basic unitary apportionment approach, albeit with a number of local variations, that the National Conference of Commissioners on Uniform State Laws drafted the model Uniform Division of Income for State Tax Purposes Act (UDIPTA). *See* G. Danvers, *State Income Taxation of Multijurisdictional Corporations: An Historical Perspective*, 22 Duquesne Law Rev. 937, 954-55 (1984). UDIPTA, and its successor Multistate Tax Compact, which embodies UDIPTA's principles, is by far the dominant method of corporate income taxation under State laws. *See* Hellerstein Treatise, ¶ 9.06 and Table 9-2, at 9-24.

practice, it would be for us now to abandon our settled jurisprudence defining the limits of state power to tax under the unitary business principle." *Id.*[8]

The unitary apportionment method has at least three major advantages over the separate accounting system when applied to multijurisdictional businesses. First, the unitary method captures the added wealth and value resulting from economic interdependencies of multistate and multinational corporations through their functional integration, centralization of management, and economies of scale. A unitary business also benefits from more intangible values shared among its constituent parts, such as reputation, good will, customers and other business relationships. *See, e.g., Mobil*, 445 U.S. at 438-40; *Container*, 463 U.S. at 164-65. Separate accounting, with its emphasis on carving out of the overall business only income from sources within a single State, ignores the value attributable to the integrated nature of the business. Yet, to a large degree, the wealth, power, and profits of the world's large multinational enterprises are attributable to the very fact that they are integrated, unitary businesses. Hellerstein Treatise, ¶ 8.03 at 8-32.[9]

[8] The dissenting justices in *Allied-Signal*, though disagreeing with the majority's application of unitary business standards to the case, also expressly declined to abandon the unitary business principle, recognizing that to do so would open the door to "a corporate shell game to avoid taxation," by allowing taxpayers to engage in "manipulations of corporate structure" to take advantage of separate accounting and the differing tax rates of various jurisdictions in which the unitary business operates. 112 S.Ct. at 2265 (O'Connor, J., joined by Rehnquist, C.J., Blackmun, J., and Thomas, J., dissenting). *See generally* Mirage, *A Solidification of the Unitary Business Principle: Allied-Signal, Inc. v. Director, Division of Taxation*, 46 Tax Law. 541 (1993).

[9] As one commentator has explained:

> To believe that multinational corporations do not maintain an advantage over independent corporations operating within a similar business sphere is to ignore the economic and political strength of the multinational giants. By attempting to treat those businesses which are in fact unitary as independent entities, separate accounting "operates in a universe of pretense; as in Alice in Wonderland, it turns reality into fancy and then pretends it is the real world."

(continued...)

Second, the unitary principle avoids the pitfalls inherent in separate accounting's attempt to determine what prices and values to ascribe to the so-called "arms-length" transactions among parent, subsidiary, and affiliated corporations. Since, for many unitary business groups, insufficient data exists from the open market to impute transfer prices with any reasonable degree of accuracy, the potential for deliberate manipulation by multinational enterprises and large errors in income reporting inevitably exists under the separate accounting system. Hellerstein Treatise, ¶ 8.03, at 8-29, 8-30; G. Weissman, note 10, *supra*, at 51. Apportionment by formula under the unitary business principle does not rely on these sorts of theoretical transfer price calculations and thus avoids errors inherent in the formal separation of what are in fact intra-corporate group transfers. *See Allied-Signal*, 112 S.Ct. at 2261; *Container*, 463 U.S. at 164-65.

Third, separate accounting is extremely expensive for States to administer when applied to unitary businesses because of the need to trace "the myriad of transfers which take place daily, monthly, yearly ...." Hellerstein Treatise, ¶ 8.03, at 8-29; G. Weissman, note 10, *supra*, at 52. Thus, separate accounting has been unpopular with state legislatures and "has become ever less viable in practice and more dubious in principle." Hellerstein Treatise, ¶ 8.03 at 8-29, & n.101.

Barclays concedes that it is a unitary business. Pet. Br. 3; JA-16. Indeed, there are few businesses today in which value is more integrated, more "fluid" among jurisdictions, than international banking and financial services. Both the capital and the expertise of that industry can be and is deployed, to a significant extent, without regard to geographical boundaries, much less corporate structure.[10] Thus, Barclays is a classic subject for taxation by the

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[9](...continued)
G. Weissman, *Unitary Taxation: Its History and Recent Supreme Court Treatment*, 48 Albany L. Rev. 48, 50-51 (1983), *quoting* Hellerstein, *The Unitary Business Principle and Multicorporate Enterprises: An Examination of the Major Controversies*, 27 Tax Exec. 313, 317 (1975).

[10] A sampling of reported cases gives a sense of the transjurisdictional scope of Barclays' business. *See, e.g., Torwest DBC, Inc. v. Dick*, 810 F.2d 925 (10th
(continued...)

unitary apportionment method which, as discussed *supra*, the Court has long recognized to be not only constitutionally permissible, but in many respects conceptually preferable, for such businesses.

II. *CONTAINER* AND *WARDAIR* COMPEL AFFIRMANCE OF THE CALIFORNIA SUPREME COURT'S UNANIMOUS DECISION UPHOLDING UNITARY APPORTIONMENT OF BARCLAYS' TAX.

Barclays makes only one argument under the Court's basic four-part framework for Commerce Clause review, first articulated in *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977), and expressly extended to this Foreign Commerce Clause context in *Container*, 463 U.S. at 165-66, 170-72 (1983). Barclays argues that its alleged costs of complying with the tax amount to "discrimination" against foreign commerce. California is better situated to respond to that argument than the *amici* States, given its superior knowledge of its taxation scheme and the record below. For that reason, and because Barclays' "discrimination" claim is both foreclosed by *Container* and unsupported by any of the Court's other Commerce Clause tax decisions, *amici* will not address that argument. Instead, their discussion will focus on Barclays' arguments based on the Court's two additional Foreign Commerce Clause concerns.

Where a State tax implicates foreign commerce, the Court addresses two additional considerations. "The first is the enhanced risk of multiple taxation." "The second ... is the possibility that a state tax will 'impair federal uniformity in an area where federal uniformity is essential.'" *Container*, 463 U.S. at 185-86, *quoting Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 447-48

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[10](...continued)
Cir. 1987) (loans by Barclays' Canadian affiliate to Colorado business); *Barclays Discount Bank Ltd. v. Levy*, 743 F.2d 722 (9th Cir. 1984) (loans by Barclays Israeli affiliate to two California diamond merchants); *Barclays Bank D. C. O. v. Mercantile Nat'l Bank*, 481 F.2d 1224 (5th Cir. 1973) (loans by Barclays New York affiliate for Caribbean development project, involving companies in Atlanta, and the West Indies); *Waterways Limited v. Barclays Bank PLC*, 571 N.Y.S.2d 208 (App. Div. 1991) (hotel financing loan by Barclays, "a British banking corporation, authorized to do business in New York," to Bermuda corporations).

(1979). Barclays argues that California's unitary apportionment tax ran afoul of both these Foreign Commerce Clause concerns.

Barclays' arguments are soundly foreclosed by *Container* and the Court's subsequent decision in *Wardair Canada Inc. v. Florida Dept. of Revenue*, 477 U.S. 1 (1986). The California Supreme Court's reliance on *Wardair* in unanimously rejecting Barclays' arguments was entirely justified. *Wardair* is analytically parallel to this case as regards the factors relevant to Barclays' Foreign Commerce Clause challenge, and fully supports the California court's decision. *Wardair* thus deserves detailed attention.

In *Wardair*, a Canadian air carrier challenged a Florida sales tax on aviation fuel used by the carrier solely for international flights to and from Florida. The Florida Supreme Court, reversing the trial court, held that a U.S.-Canadian Agreement did not preempt the State tax, and that the tax was valid under the Foreign Commerce Clause because the Agreement's limitation only on national taxes reflected the Federal Government's decision not to prohibit States from imposing such taxes. Thus, the Court rejected the contention that the tax "prevents our federal government from speaking with one voice." *Department of Revenue v. Wardair Canada, Ltd.*, 455 So. 2d 326, 329 (Fla. 1984).

In an opinion written by Justice Brennan for a seven person majority, this Court affirmed the Florida Supreme Court, ruling that the Florida tax was not preempted by federal law and did not violate the Foreign Commerce Clause. While *Wardair* involved a tax on aviation fuel, not a corporate income tax, its clarification of the Foreign Commerce Clause analysis is directly pertinent. *Wardair* compels the conclusion that the Court's earlier decision in *Container* upholding the application of California's unitary tax to a multinational unitary business with a parent incorporated in the United States should also extend to Barclays, a multinational unitary business with a parent incorporated outside of the United States.

While *Container* did not present, and therefore left open, the question whether its ruling would control where a multinational unitary business has a foreign parent, the logic of *Container* fully applies to Barclays. Thus, understanding its need to distinguish *Container*, Barclays argues that California's unitary tax is unconstitutional because it has been objected to by prior

Administrations of our Federal Government (though not by the present Administration)[11] and by other nations.

Wardair rejected the same argument. *Wardair* was explicitly not a negative or dormant Commerce Clause case, but instead set clear standards for determining whether the lawmaking actions of the Federal Government should be considered to imply permission for a particular State tax. In doing so, *Wardair* reaffirmed Congress' controlling role in Commerce Clause analysis. *Wardair* thus rejected the notion, derived by some from *dicta* in *Container*, that a State tax is invalid under the Foreign Commerce Clause simply because the tax is considered by the Executive Branch to be inconsistent with international practices and to present an impediment to the conduct of foreign affairs.

The United States filed a brief supporting Wardair's request for review by this Court. Brief for the United States as *Amicus Curiae*, No. 84-902 (filed Sept. 17, 1985) (hereinafter "*Wardair* U.S. *Amicus Curiae* Br. I"). The United States took the position that Florida's tax was "inconsistent with strongly articulated federal policy in this area and with accepted international practice," and argued that, under *Japan Line*, the tax "should be invalidated." *Id.* at 9, 22-35. The United States further argued that international aviation was governed by a pattern of treaties and other agreements which recognized a "policy" of exemptions for "instrumentalities of international air traffic," including aviation fuel, from taxes levied by both national governments and their political subdivisions. The United States said that this policy was recognized by a 1966 Resolution of the International Civil Aviation Organization, and had been "substantially implemented" by "virtually all nations" party to the Chicago Convention, a major international aviation convention to which the United States and 156 other nations were parties (hereinafter "ICAO Resolution"). *Id.* at 10-13. The United

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[11] Prior Administrations objected to the tax on "policy" grounds and thus supported Barclays' constitutional challenges to the tax in the California courts. However, the present Administration filed an *amicus* brief urging this Court not to accept review of the California courts' decisions rejecting those challenges to the tax. The Administration also has not filed an *amicus* brief in this Court supporting Barclays. Barclays' position is now little different from that of the taxpayer in *Container*. *See Container*, 463 U.S. at 195-96 ("Executive Branch has decided not to file an *amicus curiae* brief in opposition to the state tax").

States admitted that tax exemptions actually required by binding international aviation agreements were limited to "national" taxes. However, it noted that bilateral agreements and international aviation convention policies required the United States to "use its best efforts" to secure exemptions from taxes levied by State authorities. The result, the United States said, was a "very strong" expression of federal policy against taxes such as Florida's. *Id.* at 16-20.

Before Florida enacted the tax, the State Department wrote to the Florida Department of Revenue, objecting to the proposed tax and complaining that the tax would undermine the international system of reciprocal tax exemptions, "an important matter affecting U.S. international relations." The Federal Government later received diplomatic notes from approximately twenty-five foreign countries objecting to the aviation fuel tax. Those notes "uniformly" pointed to the "international consensus" and "established international practice" of granting reciprocal tax exemptions under the 1966 ICAO Resolution and bilateral aviation compacts. Some of those notes explicitly raised the possibility of retaliatory taxation. They urged the Federal Government to take the steps necessary to eliminate the Florida tax, because of the "damage that a proliferation of such taxes would cause to international aviation." *Id.* at 20-22 & App. 1a-58a.

After this Court accepted review in *Wardair*, the United States filed a second brief on the merits supporting Wardair's challenge to the Florida tax. Brief for the United States as *Amicus Curiae* in Support of Appellant, No. 84-902 (filed Dec. 26, 1985). That brief reiterated the arguments stated in the United States' first *amicus* brief and stressed the concerns that: the tax would invite retaliatory taxation against U.S. air carriers which would be felt by the nation as a whole; that U.S. carriers might be subjected to a variety of other discriminatory measures abroad; and that the tax would undercut negotiations by the United States with other nations to rectify such discrimination, frustrating the federal objective of achieving and maintaining reciprocal tax advantages. *Id.* at 9-10.

A. Under *Wardair*, A Federal Policy Must Have The Force Of Law To Invalidate A State Taxation Method.

In *Wardair*, the United States and other *amici* made the same argument that Barclays makes here: that "federal policy" required invalidation of the tax.[12] That policy, they argued, was "manifested" by international practices reflected in (1) a Chicago Convention on International Civil Aviation, to which the United States and 156 other nations were parties; (2) the Resolution, adopted November 14, 1966, by the ICAO, an organization of which the United States is a member; and (3) more than 70 bilateral agreements dealing with international aviation into which the United States had entered with various foreign countries.

The Court rejected that contention in *Wardair*. The Court noted that there was an "international aspiration" to eliminate such State taxation of international aviation, but held that "the law as it presently stands acquiesces in taxation of the sale of fuel by political subdivisions of countries."[13] The Court's conclusion was based principally on the fact that while the United States was a party to the Chicago Convention and more than 70 aviation treaties, "in not one of these agreements has the United States agreed to deny the States the power asserted by Florida in this case." *Wardair*, 477 U.S. at 11. That ruling could not be more pertinent here. As discussed *infra*, in <u>none</u> of the numerous income tax treaties to which the United States is a party has it agreed to "deny the States the power" to use worldwide unitary apportionment in their corporate tax schemes.

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[12] More than 40 international air carriers filed *amicus curiae* briefs in *Wardair* urging the Court to invalidate the Florida tax.

[13] *Wardair* made it clear that international opposition to a State tax as "inconsistent" with international practices, conventions, or resolutions cannot serve to invalidate the tax, absent some prohibition having the "force of law." 477 U.S. at 10-12. The Court recently reemphasized this point in *Itel Containers Int'l Corp. v. Huddleston*, 113 S.Ct. 1095 (1992), where it refused to invalidate a State tax on international container leases, politely declining the requests of several nations to do so in light of "international practices." <u>Id</u>. at 1100-01 ("with all due respect" to other nations' positions, the Court adheres to the view that Container Conventions do not prohibit tax challenged by Itel).

The Court acknowledged that the ICAO Resolution "undeniably does endorse an international scheme whereby fuel would be exempt" from a State tax like that imposed by Florida. *Id.* at 11. However, the Court refused to consider that Resolution to establish a federal policy sufficient to invalidate the tax, because it "has not been specifically endorsed, let alone signed, entered into, agreed upon, approved, or passed by either the Executive or Legislative branch of the Federal Government. In other words, no action has been taken to give the Resolution the force of law." *Id.* at 12. That principle applies in this case: no federal "policy" having "the force of law" prohibits State worldwide unitary taxation.

B. Congress May, By Negative Implication, Permit A State Tax Affecting Foreign Commerce, Eliminating The Need For Negative Foreign Commerce Clause Review.

Equally critical in this case is *Wardair's* ruling upholding the Florida tax on the grounds that Congress "affirmatively acted, rather than remained silent, with respect to the power of the States to [impose the tax], and thus that the case does not call for dormant Commerce Clause analysis at all." *Wardair*, 477 U.S. at 9. That ruling was not based on express authorization by Congress, but on the "negative implications" drawn from aviation treaties and conventions. The Court reasoned that "the negative implications of [provisions of the Chicago Convention] support recognizing Florida's power to tax; certainly, the provision demonstrates the international community's awareness of the problem of state and local taxation of international air travel, specifically aviation fuel, and represents a decision by the parties to that Convention to address the problem by curtailing and limiting only some of the localities' power to tax, while implicitly preserving other aspects of that authority." *Id.* at 10.

Similarly, "[b]y negative implication arising out of more than 70 agreements entered into since the Chicago Convention, the United States has at least acquiesced in state taxation of fuel used by foreign carriers in international travel." *Id.* at 12. The Court found especially persuasive the fact that an agreement between the United States and Canada, Wardair's corporate domicile, was among those that "acquiesced" in such State taxation. *Id.* at 11-12. The Court

held that these "negative implications" supported the conclusion that Congress had "affirmatively decided to permit the States to impose these sales taxes on aviation fuel." The Court held that it thus did not even need to reach the issue whether negative Foreign Commerce Clause analysis would require invalidation of the Florida tax. *Id.* at 12-13.

C. Congress Has Repeatedly Been Presented With The Issue Whether States Should Be Prohibited From Taxing Multinationals On A Worldwide Unitary Basis, And Has Repeatedly Declined To Do So.

There is no doubt that similar "negative implications" from Congress' consideration of income tax treaties and legislation compel the conclusion here that Congress must be considered to have decided to permit States to tax multinational unitary businesses using worldwide unitary apportionment.

1. United States Income Tax Treaties Reserve State Taxation Authority Over Foreign Multinationals.

The Executive Branch may well have had foreign policy concerns with State worldwide unitary taxation and may well have sympathized with complaints by other nations, notably the United Kingdom, about that taxation method. However, the U.S. Model Income Tax Treaty and <u>every</u> income tax treaty ratified by the United States reflect a clear federal policy that a State's right to use that tax method should not be surrendered to international criticism, even in the name of international conformity.

The U.S. Model Income Tax Treaty, adopted in 1977, provides that only taxes imposed by the United States at the <u>federal</u> level are governed by treaty provisions that affect unitary taxation. 1977 U.S. Model Income Tax Treaty, Art. 2., *reprinted in* 5 R. Rhoades & M. Langer, Income Taxation of Foreign Related Transactions, §92.02 (1993) (hereinafter "Rhoades & Langer"). A proposed new Model Treaty, the 1981 Draft U.S. Model Income Tax Treaty, similarly extended such restrictions only to federal taxes. *Id.*, §93.02. Both Models were used as the basis for United States

income tax treaty negotiations. Neither imposes <u>any</u> restraint on unitary taxation by the States.[14]

The absence of such restraints on State taxes was not inadvertent. Assistant Secretary of the Treasury for Tax Policy, Donald Lubick, testifying before the U.S. Senate with respect to the United States-United Kingdom Treaty, explained that the U.S. Model Treaty was intentionally drafted so that "local U.S. taxes are not covered because it is unlikely that the United States would consent to the ratification of any treaty provision that restricted the rights of the ... states to impose their own taxes." International Tax Treaties: Hearing Before the Sen. Com. on Foreign Relations, 96th Cong., 1st Sess., at 112 (1979).[15]

Consistent with the policy reflected in the U.S. Models, <u>none</u> of the income tax treaties approved by the U.S. Senate and ratified has included any restrictions on the right of States to impose corporate income taxes on a worldwide unitary basis. There are currently more than forty-five such treaties in force. *See* 3 Rhoades & Langer, *supra*, §15.00 *et seq*., §16.11.

It is important to note that a number of treaties cover certain sub-national taxes of the other nation, though covering only "Federal" taxes of the United States. Such treaties are in force, for

[14] During the Senate's consideration of the United States-United Kingdom Treaty, discussed *infra*, the Treasury Department explained that it had used an informal "model" as the basis for negotiations for years. In 1976, a decision was made to codify the U.S. Model; it was published the following year. The Model treaty was "sent to potential treaty partners prior to the commencement of negotiations," and served "as the discussion draft during the first round of negotiations." S. Exec. Message Q, 96th Cong., 1st Sess., App. C, at 45 (1979). While the 1981 Draft Model was never finalized, it was used as the "actual" U.S. Model in some negotiations. 5 Rhoades & Langer, *supra*, §93.00.

[15] The U.S. Model Treaty was published following the 1977 publication of a revised Model Convention by the Organization of Economic Cooperation and Development ("OECD"), of which the United States is a member. The U.S. Treasury revised the U.S. Model to conform to the OECD Model, "where possible." S. Exec. Message Q, 96th Cong., 1st Sess., App. C, at 45 (1979). The 1977 OECD Model covers both national taxes and those imposed by a nation's "political subdivisions or local authorities." 5 Rhoades & Langer, *supra*, §90.02. Again, the decision that the U.S. Model would not cover State taxes reflects a clear policy decision. It is one of the "important differences between the two models." *Id.*, §§94.00, 94.02 (comparison of OECD and U.S. Models).

example, between the United States and Belgium, China, Finland, Iceland, Italy, Norway, Sweden and Switzerland.[16] Those treaties were entered into over a long period of time, both before and after the U.S. Senate's consideration of the United Kingdom treaty. They reflect the fact that the United States has long been well aware of the issue of extending tax treaty restrictions to sub-national, including State, taxes. They highlight the <u>policy</u> of the United States, embodied in the U.S. Models and every ratified U.S. income tax treaty, not to agree to any such restrictions on the States.

The only tax treaty that the United States even considered ratifying which included restraints on State unitary taxation was the United States-United Kingdom treaty known as the Convention for the Avoidance of Double Taxation ("UK-2 Treaty"). *See* 124 Cong. Rec. S18404, S18408, S18421 (1978) (proposed treaty's coverage of State taxation was a "new provision, not found in other United States tax treaties"). Article 9, section 4 of the treaty, as originally transmitted to the Senate for advice and consent, "would have limited the rights of States to tax British multinationals using the worldwide combination unitary method of apportionment of income." Staff of Joint Comm. on Taxation and Senate Comm. on Foreign Relations, 96th Cong., 1st Sess., Tax Treaties: Steps in the Negotiation and Ratification of Tax Treaties and Status of Proposed Tax Treaties 4-5 (Joint Comm. Print 1979).

The Senate held hearings and extended debates concerning the relative merits of unitary and separate accounting apportionment methodologies, the States' use of unitary apportionment, and the

[16] *See* Belgium, T.I.A.S. No. 6073, Art. I, (entered into force Aug. 29, 1966) (covers "communal supplemental" taxes); China, K.A.V. 313, Art. 2 (entered into force Jan. 1, 1987) (covers "local income tax"); Finland, T.I.A.S. No. 7042, Art. 1, (entered into force Feb. 28, 1971) (covers "communal tax"); Iceland, T.I.A.S. No. 8151, Art. 1 (entered into force Dec. 26, 1975) (covers "municipal income tax"); Italy-2, T.I.A.S. No. 11064, Art. 2 (entered into force Nov. 30, 1985) (covers "local income tax"); Norway-2, T.I.A.S. No. 7474, Art. 1 (entered into force Nov. 29, 1972) (covers "municipal taxes on income," as well as "municipal taxes on real property"); Sweden-1, T.S. 958, 11 Bevans 809, Art. I (entered into force Nov. 14., 1939) (covers "communal income tax"); Switzerland-1, T.I.A.S. No. 2316, Art. I (entered into force Sept. 27, 1951) (covers "federal, cantonal and communal taxes on income").

appropriateness of restricting the States from using that tax method in the UK-2 treaty. *See, e.g.*, 124 Cong. Rec. S16892-99, S18400-30, S18651-70, S18665-67 (1978). The Senate refused to consent to the Treaty with those restrictions on the States, instead reserving its consent pending renegotiation of relevant provisions to preserve State taxation rights. *See* 124 Cong.Rec. S18670, S19076 (1978) (Senate consent with reservation by 82 to 5 vote). The Third Protocol to the Treaty thereafter negotiated limited its scope to "Federal income taxes." 31 U.S.T. 5669, 5709-13; T.I.A.S. No. 9682. The Senate was assured that the Treaty thus would not restrict the States from using worldwide unitary apportionment to tax British-based businesses. S. Exec. Message Q, 96th Cong., 1st Sess., App. B, at 33 (1979) (Treasury Department Technical Explanation of Third Protocol). With the Protocol eliminating that restriction on State taxes, the Senate consented to ratification. 125 Cong. Rec. S17434, S17796 (1979) (Protocol consented to by vote of 98-0). *See also* Staff of Joint Comm. on Taxation and Senate Comm. on Foreign Relations, 96th Cong., 1st Sess., Explanation of Proposed Third Protocol to Proposed Income Tax Treaty Between the United States and the United Kingdom 1 (Joint Comm. Print 1979).

As in *Wardair*, a "negative implication" clearly must be drawn from the U.S. Model Treaties, the many income tax treaties into which the United States has entered, and the UK-2 Treaty. Federal policy, as reflected in foreign policy conduct having the "force of law," has consistently been to retain for the States the right to use worldwide unitary apportionment for corporate taxation, despite the objections to that taxation method by other nations.

And, as in *Wardair*, "most strikingly," the Treaty with the United Kingdom, home to Barclays' parent, does not constrain such State taxation. That "omission ... must be understood as representing a policy choice" not properly overridden by the Court through negative Foreign Commerce Clause analysis. *Wardair*, 477 U.S. at 11-12.

2. Congress Has For Years Refused To Pass Legislation Restricting State Unitary Taxation Of Multinationals.

Barclays argues that its position is supported by the fact that one reason for the Senate's refusal to consent to the original UK-2 Treaty was the view that such restrictions on State taxation rights should not be effected through the treaty process, but instead, if at all, through the normal Congressional legislation process. However, that view merely reflects the Senate's understanding that the proposed restriction on State taxation involved an extremely significant issue of States' rights under our federal system.

The States' sovereign right to devise their own taxation systems is deeply imbedded in the Constitution. During the debate over ratifying the Constitution, for example, Alexander Hamilton wrote that "the individual States should possess an independent and uncontrollable authority to raise their own revenues." With the exception of import and export duties, States "retain [the authority to tax] in the most absolute and unqualified sense; and ... an attempt on the part of the national government to abridge them in the exercise of it would be a violent assumption of power." A. Hamilton, The Federalist, No. 32, at 197-98 (Rossiter ed. 1961).

The Senate's refusal to consent to the UK-2 Treaty without the Protocol excepting State taxation from coverage thus reflected constitutionally appropriate respect for State taxation authority. It was also not an aberration of Congressional policy. Over the ten year period preceding the Senate's consideration of that Treaty, several bills were introduced in Congress that would have restricted unitary apportionment by the States. *See* 124 Cong. Rec. S18416 (1978). Contemporaneously with the Senate's consideration of the UK-2 Treaty, similar bills were introduced that would have effected such restrictions. 125 Cong. Rec. 1748 (1979); S. 983, 96th Cong., 1st Sess. (1979). No such legislation progressed far in Congress and, obviously, none was enacted.

Thereafter, in *Container*, this Court recognized that "Congress has long debated, but has not enacted, legislation designed to regulate state taxation of income," and that at that time there was "pending one such bill of which we are aware." *Container*, 463 U.S. at 196-97, *citing* H.R. 2918, 98th Cong., 1st Sess. (1983). Since *Container*, a series of bills have been introduced in Congress

to prohibit States from taxing multinational corporations on a worldwide unitary apportionment basis. Similar legislative efforts have been made through proposed amendments to general trade legislation. One recent such bill was introduced in the Senate with specific reference to this case and its litigation status in the California courts. *See* 137 Cong.Rec. S13979-81 (1991) (introduction of S. 1775). That bill was simply the latest in a long line of unsuccessful legislation proposing to restrict State unitary taxation, including bills introduced by the Reagan Administration in the years after *Container*.[17]

Succeeding Congresses have considered these bills. Hearings have been held at which Congress has heard testimony both favoring and opposing restricting State worldwide unitary taxation. The objections of other countries and concerns about international trade and investment, as well as the possibility of retaliation, have

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[17] President Reagan instructed the Solicitor General not to file an *amicus* brief supporting Container. *See* 20 Tax Notes 901 (Sept. 12, 1983). At that time, President Reagan also did not support federal legislation restricting the taxing powers of the States. Instead, then Secretary of the Treasury Regan appointed a committee to try to resolve the controversy. The resulting Working Group on Worldwide Unitary Taxation, consisting of eighteen governors, chief executive officers, State legislators and other officials, considered issues raised by the unitary method and attempted to agree upon an alternative. After ten months, their final report recommended only that three general principles guide state tax policy, leaving, among other things, the question of taxation of dividends received from foreign corporations to be decided on a state-by-state basis. *See* Miller, A State Perspective on the Worldwide Unitary Taxation Working Group and Task Force, (Part 1 of 3), 1985 Multistate Tax Commission Review 1-9 (November 1985). *See generally* U.S. Department of the Treasury, The Final Report Of The Worldwide Unitary Taxation Working Group (August 1984).

After the Working Group failed to resolve the issue, the Reagan Administration decided to introduce legislation restricting State unitary taxation to a particular "water's edge" formula. 22 Tax Notes 244-45, 670, 1202 (1985). *See* 131 Cong.Rec. S17970 (1985) (introduction of S. 1974 on behalf of Administration); 131 Cong.Rec. H5754 (1985) (introduction of same, as H.R. 3980, in House). Many other bills have been introduced since *Container* that proposed to restrict the States' use of unitary taxation. *See, e.g.*, 135 Cong.Rec. S6331-32 (1989) (S. 1139); 135 Cong. Rec. H780 (1989) (same bill introduced in House); 133 Cong.Rec. H6373 (1987) (H.R. 2990); 132 Cong.Rec. S7488 (1986) (proposed amendment No. 2080 to Tax Reform Act of 1986); 131 Cong.Rec. S5924 (1985) (S. 1113); 131 Cong.Rec. S3170 (1985) (S. 687).

been heard by Congress. Yet, each Congress has declined to enact any such legislative proposals.

Barclays has little response to what the California Supreme Court, in its decision in this case, rightly termed "the din of a 'governmental silence' that cannot be ignored." *Barclays Bank Int'l Ltd. v. Franchise Tax Bd.*, 829 P.2d 279, 294 (Cal. 1992). Barclays' lament that no restrictive legislation has even been voted out of committee merely undercuts its argument. Barclays Br. 9. Two possible conclusions flow from Congressional inaction, over 20 years, with respect to such proposed legislation: 1) Congress does not view the "international furor," in Barclays' phrase, concerning unitary taxation to be sufficiently important even to warrant advancing such legislation to a vote; or 2) Congress may share some concern with that "furor," but considers State taxation rights under our federal system to greatly outweigh that concern.

The same conclusion must be drawn from the record of Congress' consideration of proposed legislative restrictions on State unitary taxation as from the facts concerning U.S. income tax treaties: Congress has decided to allow the States to continue to employ the worldwide unitary taxation method, despite objections by other nations and some Administrations. Congress has chosen not to exercise its constitutional authority to prevent the States from using that method to tax both domestic and foreign-domiciled multinationals. Again, in *Wardair's* terms, Congress should be considered, by "negative implication," to have "affirmatively acted, rather than remained silent, with respect to the power of the States to [use unitary taxation]," so that "the case does not call for dormant Commerce Clause analysis at all," in order to uphold California's unitary taxation of Barclays. *Wardair*, 477 U.S. at 9.

III. CALIFORNIA'S UNITARY TAXATION OF BARCLAYS WOULD ALSO BE CONSTITUTIONAL UNDER THE COURT'S "NEGATIVE" FOREIGN COMMERCE CLAUSE ANALYSIS.

Only if the Court were to conclude that Congress has not adequately revealed its intent to continue to allow State worldwide unitary taxation is it necessary, under *Wardair*, for the Court even to reach the "negative" Foreign Commerce Clause issues raised by

Barclays. Again, the two prongs of that analysis are concerned with "multiple taxation" and "the possibility that a state tax will impair federal uniformity in an area [of foreign relations] where federal uniformity is essential." *Container*, 463 U.S. at 185-86.

Amici will not respond in detail to Barclays' argument that the negative Foreign Commerce Clause's multiple taxation concern requires the Court to invalidate California's tax. *Container* rejected a "double taxation" argument indistinguishable from that made by Barclays. *Id.* at 185-93.[18] While *Container* involved a domestic, rather than a foreign parent, with subsidiaries in foreign countries and the United States, *Container's* logic concerning "double taxation" squarely refutes Barclays' argument.[19]

The only issue that might remain under "negative" Foreign Commerce Clause analysis is the question "whether California's decision to adopt formula apportionment in the international context was impermissible because it 'may impair federal uniformity in an area where federal uniformity is essential,' and 'prevents the Federal Government from "speaking with one voice" in international trade.'" *Id.* at 193 (citations omitted). *Container* further explained that "a state tax at variance with federal policy will violate the 'one voice' standard if it either implicates foreign

[18] Barclays tries to distinguish *Container* on the basis that the taxpayer there did not prove that actual double taxation resulted from California's unitary apportionment. Barclays Br. 32. However, in *Container*, California did "not seriously dispute the existence of actual double taxation, and [the Court] assume[d] its existence for purposes of [the Court's] analysis." 463 U.S. at 187 n.22. *See also id.* at 187 ("the tax imposed ... has resulted in actual double taxation, in the sense that some of the income taxed without apportionment by foreign nations as attributable to appellant's foreign subsidiaries was also taxed by California as attributable to the State's share of the total income of the unitary business of which those subsidiaries are a part").

[19] The Hellerstein Treatise convincingly argues that the "double taxation" doctrine cannot logically be applied in the context of a properly apportioned "State tax imposed alongside taxation by a foreign government," because the Court has no authority to impose limits on a foreign government's taxation scheme, or otherwise to achieve the sort of complete international tax uniformity necessary to avoid double taxation. As *Container's* analysis suggests, the Court should confine its concern to the issue of fair apportionment of an income tax, rather than chase the chimera of international "double taxation." Hellerstein Treatise, ¶8.14[4][a], at 8-143 to 8-145.

policy issues which must be left to the Federal Government or violates a clear federal directive." *Id.* at 194 (citations omitted).

Barclays has not argued that any "clear federal directive" was violated by California's unitary tax. Thus, the only remaining question is whether that tax "implicates foreign policy issues which must be left to the Federal Government."

With respect to this issue, the Court's negative Foreign Commerce Clause analysis has involved interest balancing, as the Court most explicitly acknowledged in the recent decision in *Itel Containers Inter. Corp. v. Huddleston*, 113 S.Ct. 1095, 1103-05 (1993). That facet of the doctrine has been a focus for criticism by Justice Scalia, as well as other scholars, on the basis that it lacks a sound textual and historical basis, and leads to judicial "legislation" inappropriately interfering with State sovereignty.[20] *Amici* respectfully urge the Court to adopt Justice Scalia's textually and institutionally restrained Commerce Clause views. However, in the alternative, *amici* respectfully suggest that the Court might use this case to further clarify and refine its balancing analysis.

That analysis, embodied in *Japan Line*, *Container*, *Itel*, and *Wardair* (though that decision did not undertake a truly "dormant" analysis) considers essentially four factors: 1) Congressional action concerning legislation or international agreements related to issues raised by the tax; 2) the nature of the tax itself in the context of State taxation rights and foreign affairs; 3) to a very limited extent, the Executive's Branch's views; and 4) the Court's ability to afford an appropriate remedy if it invalidates the tax. *Amici* will now summarize their views on each of these factors.

[20] *See, e.g.*, *Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue*, 483 U.S. 232, 259-65 (1987) (Scalia, J., concurring in part and dissenting in part). Justice Scalia recently summarized and expanded those views as respects foreign commerce in *Itel*, 113 S.Ct. at 1106-07 (1993) (Scalia, J., concurring). *See also* Breker-Cooper, *The Commerce Clause: The Case for Judicial Non-Intervention*, 69 Or. L.Rev. 895 (1990); Redish & Nugent, *The Dormant Commerce Clause and the Constitutional Balance of Federalism*, 1987 Duke L.J. 569; Eule, *Laying the Dormant Commerce Clause to Rest*, 91 Yale L.J. 425 (1982); Tushnet, *Rethinking the Dormant Commerce Clause*, 1979 Wis. L.Rev. 125. While the analysis of these scholars varies somewhat, each concludes that the Court's "negative" Commerce Clause doctrine should be considerably narrowed or abandoned.

A. Congressional Action With Respect To Legislation And International Agreements.

Given the Constitution's explicit grant to Congress of the authority to regulate foreign commerce, even in a "dormant" analysis the Court obviously should look first and most carefully to Congressional lawmaking efforts relevant to a challenged State tax. If a federal policy is expressed in Congressional action that has the force of law, with which the State tax is at odds, the Court should then invalidate the tax. Otherwise, it should be upheld. *See Itel*, 113 S.Ct. at 1104; *Container*, 463 U.S. at 196-97 (Court relies on failure of treaties and conventions to proscribe State taxes as primary support for decisions declining to invalidate taxes under negative Foreign Commerce Clause). *Cf.*, *Wardair*, 477 U.S. at 9-13 (foreign policy positions and international practices lacking the "force of law" rejected as basis for invalidating State tax). Even in *Japan Line*, the Court's most aggressive "dormant" case, the Court relied to a significant extent on its conclusion that a Container Convention between the United States and Japan "reflects a national policy" that <u>any</u> State property tax would "frustrate." *See also* Hellerstein Treatise, ¶8.14[5][b], at 8-147 (noting that each of the Court's "dormant" Commerce Clause State taxation decisions has looked primarily to Congressional action to determine "whether the State tax conflicts with or frustrates established Congressional policy").

As the *Wardair* discussion *supra* reveals, Congress' lawmaking conduct with respect to State worldwide unitary taxation, "by negative implication" should be considered to approve a State's right to use that taxation method, obviating the need for "dormant" Foreign Commerce Clause review. Should the Court instead reach a "dormant" analysis, that Congressional conduct makes it clear that the Court should not invalidate that taxation method, since that Congressional conduct reflects a federal policy of preserving, rather than restricting, a State's right to use that method.[21]

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[21] Barclays oddly argues that Congress' decision <u>not</u> to restrict State unitary taxation means that the Court should give effect to objections to such taxes by some foreign nations or the Executive, *i.e.*, that Congress has not "preempted" the Court from doing so. Barclays Br. 21-22. However, the only conclusion that can fairly be drawn from Congressional lawmaking decisions concerning proposed restrictions on unitary taxation by the States is that the Court should <u>not</u> use the Foreign Commerce Clause to prevent the States from using that taxation method.

B. The Nature Of The State Tax.

California's unitary corporate tax cannot be equated with the tax in *Japan Line*. The Court "deliberately emphasized in *Japan Line* the narrowness of the question presented: 'whether instrumentalities of commerce that are owned, based, and registered abroad and that are used exclusively in international commerce,'" may be subjected to property taxation by a State. *Container*, 463 at 1877, n.24. In contrast, as *Container* recognized, the tax challenged in this case merely involves California's choice of an apportionment method for attributing a part of the value of unitary business income to Barclays' business operations in California for corporate taxation purposes. However much other nations may disagree with that accounting choice, California is not thereby directly injecting itself into the conduct of foreign affairs or affronting the sovereignty of other nations.

Worldwide unitary apportionment is a tax accounting method, the choice of which may have some incidental effect on the Federal Government's conduct of foreign affairs. However, a State's choice of that well-established accounting method as best suited to its corporate taxation context, because of a policy commitment to that methodology or for administrative reasons, involves the exercise of a core right of State sovereignty, as discussed *supra*.

C. The Executive Branch's Limited Role.

Container's dicta has been viewed by some as suggesting that the Executive Branch's opposition to a particular State tax affecting foreign commerce might be sufficient to cause the Court to invalidate the tax. In fact, Barclays' argument places considerable reliance on the fact that prior Administrations provided support for its position in the California courts. As *Itel* makes clear, that reliance is misplaced.

In *Itel*, the majority opinion observed that an *amicus* brief filed by the United States supported the Court's conclusion that a State tax on lease transactions involving containers used solely in international commerce did not engender sufficient foreign policy problems to require its invalidation under the Foreign Commerce Clause. However, the Court in *Itel* stressed that the President's views were "by no means dispositive." 113 S.Ct. at 1105. Justice Scalia's concurrence and Justice Blackmun's dissent, though embracing very different views of the Foreign Commerce Clause,

also considered the President's views to be entitled to little more than persuasive weight, interestingly, for the same reason: the Commerce Clause reposes authority to regulate foreign commerce in the Congress. 113 S.Ct. at 1108, 1110.

Presidential power may be broad in a political sense, but "even for hard-nosed realists, ... the constitutional theory" of that power "cannot simply be brushed aside." Monaghan, *The Protective Power of the Presidency*, 93 Colum. L. Rev. 1, 3 (1993). The President is vested with "executive Power" by Article II, §1, of the Constitution, not independent, domestic lawmaking power.

"The President's power, if any, to issue [a domestically binding] order must stem either from an act of Congress or from the Constitution ...." *Youngstown Sheet Tube Co. v. Sawyer*, 343 U.S. 579, 585 (1952). "In the framework of our constitution, the President's power to see that the laws are faithfully executed refutes the idea that he is to be lawmaker." "And the constitution is neither silent nor equivocal about who shall make laws which the President is to execute." *Id.* at 587.

Youngstown Sheet, a Steel Seizure Case, "represents the bedrock principle of the constitutional order: except perhaps when acting pursuant to some specific constitutional power, the President has no inherent power to invade private rights; the President not only cannot act *contra legem*, he or she must point to affirmative legislative authorization when so acting." Monaghan, 93 Colum. L.Rev. at 10 (footnote omitted). That case's "premise is fully applicable to presidential conduct in foreign as well as domestic affairs: no independent, free-standing presidential law-making authority exists insofar as the rights of American citizens are concerned." *Id.* at 4 (footnotes omitted).

> Thus, whatever the range of autonomous presidential authority in the foreign affairs context, presidential authority stops well short of an independent, free-standing law-making authority. Nor has the President acquired such authority by prescription. Professor Henkin rightly observes that "[n]o one has suggested that under the President's 'plenary' foreign affairs powers he can, by executive act or order, enact law directly regulating persons and property in the United States."

Id. at 49 (footnotes omitted), *quoting* L. Henkin, Foreign Affairs and the Constitution 57 (1972). These well-established principles also clearly apply to "law-making" that might limit the sovereignty of the States.

The Executive Branch lacks domestic constitutional authority to unilaterally "make laws" prohibiting taxation by the States, other than in the context of regulations or other Executive action authorized by Congress. No such authorization is present here. The only other manner in which the Executive can "make law" preempting State laws is through its role in negotiating a treaty, consented to by the Senate and ratified as law,[22] or though a valid executive agreement with a foreign nation.[23] Obviously, there is neither a treaty nor an executive agreement through which the Executive "made law" here that invalidates the California tax.

Barclays' argument with respect to this issue of Executive authority turns preemption analysis on its head. It argues that State unitary taxation intrudes into an "inherently federal area," that the Federal Government has "exclusive" authority where any "state action interferes with the conduct of foreign affairs," and that the Constitution "preempts" any such State action. Barclays Br. 41-42. To the contrary, the Constitution clearly does not, in preemption terms, "occupy the field" and nullify any State tax that might

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[22] A ratified treaty limiting State taxation would void or limit contrary State law under the express terms of the Supremacy Clause, Article VI, §2 of the Constitution.

[23] "The president can make executive agreements only in the areas where he has exclusive constitutional authority: administrative procedure, recognition of foreign sovereigns, and military affairs." S. Millet, The Constitutionality Of Executive Agreements: An Analysis Of United States v. Belmont 174 (1990). *Accord*, L. Henkin, Foreign Affairs and the Constitution 56-65 (1972) (only agreements within zones of exclusive presidential authority have effect of law); Restatement (Third) of the Law of Foreign Relations of the United States, §303(4) (1987) ("President, on his own authority, may make an international agreement dealing with any matter that falls within his independent powers under the Constitution").

Congress has primary constitutional authority for the regulation of foreign commerce and for any legislation concerning State taxation. Thus, the President certainly cannot be said to have "exclusive" or "independent" constitutional authority in that area, and serious doubts exist whether the President could constitutionally agree to restrict State income taxation schemes by executive agreement not approved as a treaty by the Senate or by Joint Resolution of Congress. *See, e.g.*, Berger, *The Presidential Monopoly of Foreign Relations*, 71 Mich. L.Rev. 1, 39 (1972) (Constitution's structure of checks and balances negates view that President may use executive agreement to address unlimited range of subjects, bypassing Senate consent process required for treaty).

implicate foreign affairs.[24] Instead, obviously, the Constitution merely gives the Congress, by virtue of its authority to regulate foreign commerce, the power to preempt such State action through legislation. *See, e.g., Wardair*, 477 U.S. at 5-7.

Respect for the Executive's in foreign affairs cannot support extension to the Executive of the power to invalidate a State taxation scheme by decree or fiat on grounds of Executive "policy." That "policy" must have a basis in legislation or other form having the "force of law. Thus, as in *Itel* and *Container*, the Executive's view that a State tax does not impermissibly interfere with the conduct of foreign affairs (or a neutral view of the tax) may provide some level of comfort for a decision upholding the tax. However, to give significant weight to the Executive's views concerning a State tax would ignore the limited nature of Presidential lawmaking authority, as *Wardair* implicitly recognized. Whatever the past or present Administrations' policy positions concerning California's unitary tax might be, those positions can provide no real support for Barclays' challenge.

D. The Court's Ability To Provide A Meaningful Remedy.

Japan Line is the only case in which the Court has struck down an otherwise valid State tax on Foreign Commerce Clause grounds. The State property tax there applied to cargo containers of Japanese shipping companies, used exclusively in foreign commerce and subjected to full value taxation in Japan. The Court held that Foreign Commerce Clause principles required invalidation of the tax, particularly in light of Container Conventions eliminating all similar taxes by signatory nations. However, a meaningful factor in the decision was the available judicial remedy: since Japan taxed the containers at full value, the Court could simply declare that the

[24] Where a State's statutes or policies do not directly inject the State into matters that are within an exclusively federal province of foreign relations with specific nations, those statutes or policies are not preempted by federal authority. State action that has only "'some incidental or indirect effect in foreign countries'" does not impermissibly intrude on the foreign relations power. *Zschernig v. Miller*, 389 U.S. 429, 432 (1968). *See also De Canas v. Bica*, 424 U.S. 351, 355 (1976) (Court rejects suggestion that "dormant foreign affairs" power invalidates state legislation that indirectly affects foreign affairs). A State's choice of a tax apportionment method, whatever its incidental effect on foreign relations, is clearly not a matter within the exclusively federal province of foreign relations as to which a State is entirely preempted from entering.

containers were not subject to any property taxation by the State. *Japan Line*, 441 U.S. at 455.

This case is very different from *Japan Line* in remedial terms. If the Court were to invalidate California's unitary apportionment method, what then? The Court should inform the States in reasonable detail what apportionment method is constitutionally required to satisfy the Court's Foreign Commerce Clause concerns, though that is an essentially legislative role. Otherwise, by logical extension of the extremist "one voice" doctrine proposed by Barclays, the States would not be able to employ any method for apportioning taxes on multinational businesses that could completely avoid foreign policy "implications" -- other than perhaps the precise method used by the multinational's "home" country.[25] In that event, a State could not adopt a single, generally applicable apportionment method -- only Congress could do so. A decision by the Court invalidating the tax would thus either entirely preempt the States from devising their own schemes for multinational taxation or surrender their sovereignty in that regard to the policies of different foreign nations. Either of these results is clearly unacceptable in light of the Court's longstanding affirmance of a State's discretion to choose its apportionment method for taxing multijurisdictional unitary businesses and the Court's repeated, wise refusal to "judicially legislate" a particular apportionment method as required by the Constitution.[26]

[25] This is what Barclays and some nations are apparently demanding. The Second Supplemental Brief of Petitioner, at 2, states its position, and that of several countries, that California's change to a "water's edge" apportionment did not resolve their objections, and that "a complete solution to the problem [requires] the establishment of the arm's length principle as the only legitimate basis to tax foreign companies in any state."

[26] *See, e.g., Trinova Corp. v. Michigan Dep't of Treasury*, 498 U.S. 358, 386-87 (1991) ("We have always declined to undertake the essentially legislative task of establishing a single constitutionally mandated method of taxation."). *Accord, Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159, 171 (1983); *Moorman Mfg. Corp. v. Bair*, 437 U.S. 267, 277-80 (1978). The Court has similarly made it clear that it "cannot infer that treatment of foreign income at the federal level mandates identical treatment by the States." *Mobil Oil Corp. v. Comm'r of Taxes of Vermont*, 445 U.S. 425, 448 (1980).

E. "Negative" Foreign Commerce Clause Conclusion.

This Court has recognized that it "has little competence in determining precisely when foreign nations will be offended by particular acts, and even less competence in deciding how to balance a particular risk of retaliation against the sovereign right of the United States as a whole to let the States tax as they please." *Container*, 463 U.S. at 194. The Court should thus exercise great restraint in its Foreign Commerce Clause review of a State tax, either by adopting Justice Scalia's doctrinally restrained view of the Commerce Clause, or by balancing the interests strongly in favor of both State sovereignty and the authority of Congress to effect foreign commerce policy through law. Should the Court undertake a balancing analysis, "[l]eft to decide whether [California's] tax rests on the *Japan Line* or the *Container Corp.* side of the scale, [the Court should] have no doubt that the analysis and holding of *Container Corp.* control." *Itel*, 113 S.Ct. at 1104.

CONCLUSION

The *amici* States respectfully submit that the decisions of the California courts in these petitions should be affirmed. California's worldwide unitary apportionment tax should be upheld as constitutional under either the Court's *Wardair* "Congressional policy" analysis or its negative Foreign Commerce Clause doctrine.

Respectfully Submitted,

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